



BEFORE THE PUBLIC UTILITIES COMMISSION OF THE  
STATE OF CALIFORNIA

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Application of Southern California Edison )  
Company (U 338-E) for a Commission Finding )  
that its Procurement-Related and Other )  
Operations for the Record Period January 1 )  
Through December 31, 2006 Complied with its )  
Adopted Procurement Plan; for Verification of its )  
Entries in the Energy Resource Recovery )  
Account and Other Regulatory Accounts; and for )  
Recovery of \$4.863 Million Recorded in Four )  
Memorandum Accounts. )

Application 07-04-001  
(Filed April 2, 2007)

**OPENING BRIEF OF SOUTHERN CALIFORNIA EDISON COMPANY (U 338-E)**

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Dated: **October 12, 2007**

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**OPENING BRIEF OF SOUTHERN CALIFORNIA EDISON COMPANY (U-338E)**

**I.**

**INTRODUCTION AND PROCEDURAL HISTORY**

Pursuant to the briefing schedule set forth in ALJ Patrick's September 24, 2007 Ruling on Submission of Proceeding for Decision (September 24th Ruling), Southern California Edison Company (SCE) hereby submits its opening brief in its April 2007 Energy Resource Recovery Account (ERRA) proceeding. On April 2, 2007, pursuant to D.02-10-062, D.03-07-029 and D.04-01-048, SCE filed an ERRA application setting forth the reasonableness of its operations for the Record Period, January 1, 2006 through December 31, 2006. In its Application, SCE seeks a finding that for the Record Period: (1) recorded fuel expenses and energy expenses were reasonable, (2) contract administration, dispatch of generation resources, and related spot market transactions complied with Standard of Conduct Four in SCE's Commission-approved procurement plan, and (3) SCE's other operations subject to Commission review were reasonable.

SCE's Application also sought a finding that the entries recorded in the Mohave Balancing Account (MBA) and related capital expenditures are reasonable and recoverable. The Commission is not reviewing SCE's MBA entries and related capital expenditures in this proceeding, however, pursuant to the June 4, 2006 Scoping Memo and Ruling of Assigned Commissioner and Administrative Law Judge (June 4th Ruling). The June 4th Ruling states that SCE must first address the permanent status of the Mohave Generating Station (Mohave), as required under Ordering Paragraph No. 9 of SCE's 2006 General Rate Case decision, D.06-05-016, before the Commission will consider this issue in an appropriate proceeding.

However, the June 4th Ruling does not preclude SCE from recovering its fuel-related costs associated with Mohave. These are set forth in Chapter Four of Exhibit SCE-1 at pages 49-53, and include costs associated with the Mohave coal supply agreement booked in 2006, as well as costs associated with SCE's standstill agreements with Black Mesa Pipeline (BMP) and Peabody. These costs are recovered through the ERRA Balancing Account and, accordingly, should be reviewed in this proceeding.

On May 24, 2007, the Commission issued Resolution E-4075, in response to SCE's Advice 2087-E, which requested the Commission to rule that the BMP standstill agreement were fuel-related costs that SCE could record in the ERRA Balancing Account. The Resolution authorized SCE to record the BMP costs in the ERRA, but also ruled that SCE should present additional evidence to demonstrate (1) that it exercised reasonable due diligence and negotiated in good faith to modify the pollution control requirements for Mohave in order to recover from ratepayers the standstill agreement costs recorded in the ERRA, and (2) that SCE had a legal obligation to pay the BMP standstill agreement costs. On June 28, 2007, SCE served supplemental testimony to address the issues raised in Resolution E-4075.

On August 3, 2007, the Division of Ratepayer Advocates (DRA) submitted its "Report on Southern California Edison Company's 2006 Energy Resources Recovery Account (ERRA)"

(Report) in this proceeding.<sup>1</sup> DRA's August 3 Report did not recommend any disallowances, but it did raise concerns relating to SCE's implementation of least cost dispatch principles and the reasonableness of SCE's nuclear generation and fuel expenses incurred during the Record Period. Regarding the second issue, DRA's August 3 Report expressed particular concern over SCE's replacement power costs associated with three outages at Unit One of the Palo Verde Nuclear Generating Station (Palo Verde). DRA stated that the reasonableness of such costs was "unclear," and that SCE should "in its testimony clarify the results of Palo Verde outages in 2006" and "demonstrate that replacement energy and other costs resulting from Palo Verde outages were reasonable."<sup>2</sup> After filing its August 3 Report, DRA served SCE with additional data requests on August 27, 2007, seeking further information regarding Palo Verde.

Before SCE could submit its rebuttal testimony addressing these issues, DRA filed concurrent motions, also on August 27, requesting: 1) bifurcation of the proceedings to address Palo Verde separately, and 2) leave to present additional testimony on Palo Verde. SCE objected that DRA's belated attempt to serve additional testimony violated Commission Rule 13.8(b). SCE also stated that its rebuttal testimony, as well as its answers to DRA's August 27 data requests, would address DRA's remaining concerns regarding Palo Verde.

SCE served its rebuttal testimony on September 7, 2007, which included substantial additional detail about the Palo Verde Unit One outages, as well as answers to the most pertinent DRA data requests.<sup>3</sup> During a September 13, 2007 conference call with ALJ Patrick and SCE's attorneys, DRA's attorneys stated that DRA was generally satisfied with SCE's rebuttal testimony and data responses, but wanted to meet informally with SCE to ask some clarifying questions regarding Palo Verde before withdrawing its motions and its request for hearings. SCE agreed to an informal meeting with DRA, and ALJ Patrick decided to hold his ruling on DRA's motions in abeyance pending a further report by the parties on September 20, 2007.

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<sup>1</sup> No other party filed testimony or otherwise participated in the proceeding.

<sup>2</sup> DRA Report at 3-7, lines 6-9 and 16-17.

<sup>3</sup> SCE served its answers to all of DRA's data requests directly on DRA on September 10, 2007.

On September 19, 2007, SCE met with DRA at its offices in San Francisco and provided DRA with detailed information addressing its concerns regarding Palo Verde. DRA was satisfied with SCE's presentation and, during a conference call with ALJ Patrick the following day, the parties agreed that DRA's bifurcation motion was moot and that evidentiary hearings were unnecessary. The parties' agreement on these issues is memorialized in the September 24th Ruling.

The September 24th Ruling states that opening briefs are due on October 12, and reply briefs on October 24, 2007. Here, in this opening brief, SCE will discuss the issues addressed in its rebuttal testimony (i.e., least cost dispatch and nuclear generation and fuel) and will briefly summarize the uncontested issues presented in the remainder of SCE's ERRA testimony. In addition, SCE has attached proposed findings of fact, conclusions of law, and ordering paragraphs in Appendix A, as required by the September 24th Ruling.

## **II.**

### **LEAST-COST DISPATCH (LCD)**

#### **1. DRA's Electric Price Comparisons**

In Chapter Two of Exhibit SCE-1 (and in the accompanying Appendices A and B), SCE shows that during the Record Period it consistently dispatched the resources and contracts under its control and made spot market transactions in a manner that complied with the Commission's adopted standard, Standard of Conduct No. Four. In Chapter Two of its August 3 Report, DRA reviewed SCE's implementation of LCD principles and found no significant deviations from the Commission's standards. Accordingly, DRA "recommend[ed] no disallowances for SCE's application of LCD principles during the Record Period."<sup>4</sup>

SCE is pleased that DRA did not recommend any disallowances. Notwithstanding DRA's recommendation, however, SCE is concerned about the "monthly average" price

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<sup>4</sup> DRA Report at page 2-8, lines 22-23.

comparison methodology utilized in DRA’s August 3 Report. This “monthly average” methodology ignores several critical distinctions involved in SCE’s spot market transactions and, as a consequence, creates the misleading implication that SCE routinely purchases electric products at the high end of the market price range and sells electric products at the low end of the market price range. SCE is concerned that DRA’s continued use of this deficient methodology could result in an unjustified disallowance recommendation in a future proceeding. Indeed, DRA’s current methodology is similar to the flawed methodology previously utilized by DRA in SCE’s April 2005 ERRA reasonableness proceeding, A.05-04-004, in which DRA recommended a \$16.36 million disallowance. The Commission rejected DRA’s methodology (and its recommended disallowance) in D.06-01-07.<sup>5</sup>

In order to avoid future disputes regarding SCE’s LCD operations, SCE addressed the shortfalls of DRA’s methodology, and the adjustments necessary to correct them, in its rebuttal testimony.<sup>6</sup> Specifically, SCE demonstrated that DRA’s average monthly price comparison is deficient because it does not purport to do any of the following: 1) account for the different prices of the various mixes of product types (CAISO<sup>7</sup> Energy, WSPP<sup>8</sup> Schedule A,<sup>9</sup> WSPP Schedule B,<sup>10</sup> or WSPP Schedule C,<sup>11</sup>) that SCE purchases and sells, 2) distinguish time frames during which SCE purchases and sells power (hour-ahead vs. day-ahead), 3) account for the different delivery locations (e.g., South of Path 15,<sup>12</sup> Palo Verde, California/Oregon Border, etc.) at which SCE purchases and sells power, or 4) consider the differences in the underlying prices of natural gas that largely drive the price of spot electricity that SCE purchases and sells.

Finally, SCE noted the following in its rebuttal testimony:

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<sup>5</sup> See D.06-01-007, at page 5.

<sup>6</sup> See Exh. SCE-4 at pages 2-7.

<sup>7</sup> California Independent System Operator.

<sup>8</sup> Western Systems Power Pool.

<sup>9</sup> Economy Energy Service.

<sup>10</sup> Unit Commitment Service.

<sup>11</sup> Firm Capacity/Energy Sale or Exchange Service.

<sup>12</sup> The CAISO area currently is divided into three zones: North of Path 15, South of Path 15, and a zonal pricing area defined as North of Path 26.

As SCE has pointed out in prior testimony and past discussions with DRA, the nature of both the historical and the current hour-ahead market does not easily lend itself to meaningful benchmarking. Moreover, the electricity spot market in California will change dramatically in the near future when the CAISO's Market Redesign and Technology Upgrade (MRTU) is implemented. This will require the utilities and the Commission staff to carefully consider an appropriate methodology for reviewing utility dispatch operations in the new MRTU environment. In the meantime, SCE looks forward to working with DRA and the other IOUs in developing an appropriate methodology for analyzing pre-MRTU spot market transactions generally, and hour-ahead transactions in particular.<sup>13</sup>

Accordingly, SCE requests the Commission to find DRA's "monthly average" methodology to be an inappropriate method for analyzing SCE's LCD operations, and to find that SCE's LCD operations comply with Standard of Conduct Four.

## **2. DRA's Statement about the Gas Market**

In its August 3 Report, DRA asserted that the Intercontinental Exchange (ICE) data available for DRA's analysis reflects "speculative" transaction prices, rather than the "intrinsic (real) value of gas."<sup>14</sup> In response, SCE's rebuttal testimony noted for the record that the price at which transactions are consummated between a willing buyer and a willing seller are, in fact, "real" market prices.<sup>15</sup> SCE's rebuttal testimony further stated that most active markets are influenced by speculators and the extent (if any) of speculators' influence on the gas market is unknowable.<sup>16</sup> In any event, SCE had a robust hedging program in place during 2006 to protect its customers from excessive price increases.<sup>17</sup>

## **III.**

### **NUCLEAR GENERATION AND FUEL**

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<sup>13</sup> Exh. SCE-4, at page 6.

<sup>14</sup> DRA Report at page 2-5, lines 16-17.

<sup>15</sup> Exh. SCE-4 at page 6, lines 19-21.

<sup>16</sup> *Id.* at lines 23-25.

<sup>17</sup> *Id.* at pages 6-7.

**A. San Onofre Nuclear Generating Station (SONGS) Record Period Generation**

SCE set forth the reasonableness of the SONGS generation and nuclear fuel expenses it incurred during the Record Period in Chapter Seven of Exhibit SCE-1. In its August 3 Report, DRA found SCE's cost of fuel reasonable and its operations "satisfactory."<sup>18</sup>

Notwithstanding its approval, DRA noted that the combined output of SONGS generation during 2006 was 26.2 percent below the combined output during 2005.<sup>19</sup> DRA, however, did not make any recommendations or findings regarding the level of SONGS generation in 2006. Instead, DRA indicated that it would review the duration of outages during 2007 in SCE's next ERRA application "to ensure this is not a recurring issue."<sup>20</sup>

Because of DRA's equivocation, SCE's rebuttal testimony provided further detail regarding the reasonableness of both the level of production and the length of outages at SONGS during the Record Period.<sup>21</sup> In particular, the rebuttal testimony pointed out that the 26.2 percent reduction in the combined SONGS output from 2005 to 2006 resulted from the fact that neither SONGS unit had a refueling and maintenance outage during 2005, whereas both units had such outages in 2006, as well as a mid-cycle maintenance outage on Unit Three.<sup>22</sup> "These factors alone were enough to account for the 26.2 percent reduction in capacity factor between 2005 and 2006."<sup>23</sup> Thus, SCE believes its rebuttal testimony sufficiently addressed DRA's concerns regarding the combined output of SONGS generation during the Record Period.

Accordingly, SCE requests the Commission to find that its generation and nuclear fuel expenses incurred for SONGS during the Record Period were reasonable.

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<sup>18</sup> DRA Report at page 3-1, lines 9-10.

<sup>19</sup> *Id.* at page 3-5, lines 5-6.

<sup>20</sup> *Id.* at page 3-5, lines 11-12.

<sup>21</sup> Exh. SCE-4 at pages 8-10.

<sup>22</sup> *Id.* at page 9.

<sup>23</sup> *Id.*



**B. Palo Verde Nuclear Generating Station (Palo Verde) Record Period Generation**

SCE also set forth the reasonableness of the Palo Verde generation and nuclear fuel expenses it incurred during the Record Period in Chapter Seven of Exhibit SCE-1. In Chapter Three of its August 3 Report, DRA reviewed SCE's Palo Verde operations and outage information during 2006 and chose not to opine on the reasonableness of SCE's costs for replacement energy at Palo Verde. Instead, DRA's August 3 Report stated only that the reasonableness of such costs was "unclear" and further stated that SCE should "in its testimony clarify the results of Palo Verde outages in 2006," and "demonstrate that replacement energy and other costs resulting from Palo Verde outages were reasonable."<sup>24</sup> After filing its August 3 Report, DRA served SCE with additional data requests on August 27, 2007 seeking further information regarding Palo Verde.

SCE began preparing rebuttal testimony addressing the concerns expressed in DRA's August 3 Report prior to receiving DRA's August 27 data requests. Before SCE could submit its rebuttal, however, DRA filed concurrent motions<sup>25</sup> requesting: 1) bifurcation of the proceedings, and 2) leave to present additional testimony regarding Palo Verde. SCE objected to DRA's motions because DRA offered no "new" evidence justifying the presentation of additional testimony and, as such, could not demonstrate "good cause" why it did not include its additional testimony in its August 3 Report as required by Rule 13.8(b) of the Commission's Rules of Practice and Procedure. SCE also objected on grounds that its rebuttal testimony, as well as its answers to DRA's August 27 data requests, would address DRA's remaining concerns.

SCE served its rebuttal testimony on September 7, 2007. SCE's rebuttal testimony provided additional detail regarding the amount and cost of its replacement power associated with the outages at Palo Verde Unit One during 2006.<sup>26</sup> In Appendix A to its rebuttal testimony, SCE attached its responses to DRA's data request No. 7.5.1, in which DRA asked SCE to state,

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<sup>24</sup> DRA Report at page 3-7, lines 6-9 and 16-17.

<sup>25</sup> DRA's motions were also filed on August 27.

<sup>26</sup> Exh. SCE-4 at pages 11-12.

(a) how much of the replacement power it purchased was related to the Unit One shutdown from January to July 2006 to deal with the vibration in the shutdown cooling valve SI-651, (b) where this replacement power came from, and (c) how much SCE paid for it.<sup>27</sup> SCE's overall testimony on this subject, plus its responses to DRA's data request contained in Appendix A, provide the Commission all the information needed to verify that the amount and cost of the replacement power associated with Unit One outages during 2006 were reasonable.

SCE's rebuttal testimony also provided additional detail regarding the nature of SCE's responsibility for Palo Verde operations.<sup>28</sup> As noted in its rebuttal testimony, SCE's oversight of the operational decisions at Palo Verde is limited. Although SCE (like the other co-owners of Palo Verde) is an NRC licensee at Palo Verde, neither SCE nor the other Palo Verde co-owners has authority to approve or disapprove operational decisions at Palo Verde.<sup>29</sup> Rather, such decisions can only be made by the plant's licensed operating agent, Arizona Public Service (APS).<sup>30</sup> Notwithstanding this limitation, SCE does employ a nuclear regulatory specialist who visited Palo Verde frequently in 2006, including during the time when Palo Verde personnel were dealing with the excess vibration on the shutdown cooling valve at Unit One. This specialist assisted SCE's management in reviewing APS' actions as APS dealt with the vibration problem, and in confirming that all actions APS took to address the problem were appropriate.<sup>31</sup>

SCE's rebuttal testimony also explained the context in which the Commission should consider in this ERRA proceeding the Nuclear Regulatory Commission's (NRC) regulation and oversight of Palo Verde.<sup>32</sup> SCE noted that the NRC's oversight is focused on safe operations, which are of paramount concern, and not on the level or cost of production.<sup>33</sup> SCE cannot interfere with decisions meant to assure the safe operation of Palo Verde in the name of

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<sup>27</sup> Appendix A to Exh. SCE-4.

<sup>28</sup> Exh. SCE-4 at pages 13-14.

<sup>29</sup> *Id.* at page 13, lines 15-16.

<sup>30</sup> *Id.* at page 14, lines 8-19.

<sup>31</sup> *Id.* at pages 13-14.

<sup>32</sup> *Id.* at pages 14-15.

<sup>33</sup> *Id.* at page 14, lines 24-26.

“maximizing production.” Any attempt to do so would be highly irresponsible and would violate NRC regulation and oversight.<sup>34</sup> With this context in mind, the first question the Commission must ask in determining whether an outage at Palo Verde was reasonable, is whether the duration of the outage was necessary to ensure safe operation and to comply with NRC safety standards. If the answer to this question is yes, then whether the cost of replacement power was reasonable is a function of the price paid for the power, not the duration of the outage.<sup>35</sup>

Furthermore, SCE’s rebuttal testimony directly addressed the NRC’s safety concerns regarding Palo Verde as expressed in its annual assessment letter of March 7, 2007:

SCE has carefully reviewed all the findings in the NRC assessment letter, and has determined that while the letter raises a number of issues regarding the safety of operations at Palo Verde during 2006, none of the concerns raised by the NRC had any impact at all on the existence or duration of any outage at any of the three Palo Verde units during 2006. In other words, the letter only raises safety issues that are within the exclusive purview of the NRC. None of the issues the NRC raised resulted in or contributed to the need for an outage, and none of the issues raised had any impact on the length of an outage. Therefore, the issues raised by the NRC had no impact on the cost of the replacement power SCE purchased during 2006 that was associated with Palo Verde outages.<sup>36</sup>

Finally, SCE’s rebuttal testimony presented substantial additional detail regarding the outages at Palo Verde Unit One during 2006.<sup>37</sup> In particular, the rebuttal testimony further detailed APS’ efforts to solve the vibration problem on shutdown cooling valve SI-651, which became excessive after APS restarted Unit One following a scheduled shutdown for the installation of new steam generators. As explained in SCE’s rebuttal testimony, solving the excess vibration problem proved to be extremely complicated and required APS to spend several months pursuing a number of alternatives, including calling in experts from both the nuclear industry and academia. APS ultimately succeeded by moving the location of the valve, which

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<sup>34</sup> *Id.* at page 15, lines 4-6.

<sup>35</sup> *Id.* at page 15, lines 17-22.

<sup>36</sup> *Id.* at page 16, lines 13-21.

<sup>37</sup> *Id.* at pages 16-31.

was a complex and challenging engineering effort. Despite having solved the issue however, APS will probably never know why the vibration problem occurred in the first place.<sup>38</sup>

SCE's rebuttal testimony also provided additional detail regarding the replacement of the pressurizer heaters in Unit One beginning on September 19, 2006, and the shutdown caused by a loose wire on a control element assembly, beginning on October 21, 2006.<sup>39</sup>

In addition to providing rebuttal testimony, SCE also responded to DRA's additional data requests, which were served on August 27, 2006. These data requests sought information pertaining to SCE's nuclear generation output, as well as information relating to the NRC's letters assessing the operation of Palo Verde. DRA's data requests were particularly focused on the latter issue. Regarding the NRC letters, DRA wanted to know the degree to which SCE exercised oversight of APS' operation of Palo Verde, and also what impact, if any, the NRC's safety concerns had on Palo Verde's power output. SCE responded to all of DRA's data requests in the answers it served on September 10, 2007.

After SCE served its rebuttal testimony and data responses on DRA, the parties had a conference call with ALJ Patrick on September 13, 2007. During the conference call, the ALJ told the parties that he had drafted a ruling in response to DRA's motions that would deny DRA's motion to bifurcate and allow DRA's additional testimony only for the purpose of background information. Before ALJ Patrick could issue his ruling, however, DRA's attorneys stated that DRA was generally satisfied with SCE's rebuttal testimony and was considering withdrawing its motions and its request for hearings. Before doing so, DRA's attorneys stated that DRA wanted to meet informally with SCE's attorneys and its rebuttal witness, Geoff Cook, to ask some clarifying questions regarding Palo Verde. SCE indicated its willingness to participate in an informal meeting with DRA, and ALJ Patrick agreed to hold his ruling in abeyance pending a further report by the parties on September 20, 2007.

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<sup>38</sup> *Id.* at pages 16-24. Because the configuration of Palo Verde Units 2 and 3 is similar to Unit 1, APS has notified the co-owners that it plans to do the same modification to Units 2 and 3 as a pre-emptive measure to prevent any possible future vibration issues at those units. *Id.*, at pages 23-24.

<sup>39</sup> *Id.* at pages 25-30.

SCE met with DRA at its offices in San Francisco on September 19, and provided DRA with additional information addressing DRA's concerns regarding Palo Verde. DRA was satisfied with SCE's presentation and, during a conference call with ALJ Patrick on the following day, the parties agreed that DRA's bifurcation motion was moot and that evidentiary hearings would be unnecessary. The parties' agreement on these issues is memorialized in the September 24th Ruling. Having resolved DRA's concerns regarding Palo Verde operations and outages during 2006, SCE requests the Commission to find that such operations were reasonable, and that the associated cost of the replacement power SCE purchased was reasonable.

## IV.

### **SUMMARY OF UNDISPUTED ISSUES**

#### **A. Hydroelectric Generation**

In Chapter Three of Exhibit SCE-1, SCE demonstrated that its hydroelectric facilities were operated in a prudent manner during the Record Period. DRA reviewed SCE's hydroelectric generation records and found that "SCE's hydroelectric generating resources [are] efficient. The efficient use and availability of SCE hydro generation resources are ensured through attentive management."<sup>40</sup>

Accordingly, SCE requests the Commission to find that its hydroelectric facilities were operated in a prudent manner during the Record Period.

#### **B. Coal Generation**

In Chapter Four of Exhibit SCE-1, SCE presented the results of its operations for SCE-owned coal-fired generating resources during the Record Period. Following a review of SCE's utility retained generation operations, DRA found these operations to be "satisfactory."<sup>41</sup> DRA's sole recommendation pertaining to coal was that "SCE should continue to strive for the lowest coal prices attainable."<sup>42</sup> SCE will continue to pursue the lowest coal prices available.

SCE's fuel related costs associated with Mohave were included in Chapter Four. These included SCE's costs associated with the Mohave coal supply agreement booked in 2006, as well as costs associated with SCE's standstill agreements with BMP and Peabody. On page 52 of Exhibit SCE-1, SCE explained that the Commission approved SCE's request to clarify that these fuel-related costs could be recorded in the ERRA balancing account.<sup>43</sup>

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<sup>40</sup> DRA Report at page 3-2, lines 26-28.

<sup>41</sup> *Id.* at page 3-1, lines 9-10.

<sup>42</sup> *Id.* at page 3-3, lines 23-24.

<sup>43</sup> Exh. SCE-1 at pages 49-54. See Tables IV-11 and IV-12. SCE's request to record the Peabody costs in the ERRA balancing account was approved in Resolution E-3981. On January 5, 2007, SCE filed Advice Letter Continued on the next page

On May 24, 2007, the Commission issued Resolution E-4075, in response to SCE's Advice 2087-E, which requested the Commission to rule that the BMP standstill agreement costs were fuel-related costs that SCE could record in the ERRA Balancing Account. The Resolution authorized SCE to record the BMP costs in the ERRA, but also ruled that SCE should present additional evidence to demonstrate (1) that it exercised reasonable due diligence and negotiated in good faith to modify the pollution control requirements for Mohave in order to recover from ratepayers the standstill agreement costs recorded in the ERRA, and (2) that SCE had a legal obligation to pay the BMP standstill agreement costs.

On June 28, 2007, SCE served supplemental testimony to address the issues raised in Resolution E-4075. In this supplemental testimony, SCE provided detailed background information regarding the circumstances surrounding the decision to suspend operations at the Mohave plant and the efforts made to resume operations after resolving the many difficult issues related to the pollution control equipment required by the federal consent decree. In December 2005, these efforts justified entering into standstill agreements with Peabody and BMP to preserve the ability to re-open Mohave should the negotiations to resolve the pollution control requirement succeed. The agreement with Peabody was signed on December 29, 2005. As to the agreement with BMP, the supplemental testimony states:

[T]he BMPI standstill agreement was not finalized in written form and signed by the parties until March 27, 2006, but BMPI's fundamental obligations to keep its facilities and staff in standstill mode through March 2007, and SCE's obligations to reimburse BMPI for that standstill, were agreed upon by SCE and BMPI by phone call and email on December 21, 2005.<sup>44</sup>

On pages 6-8 on SCE's June 28 Supplemental Testimony, SCE explains why this agreement of December 21, 2005 was contractually binding, and why it was not reduced to writing until March 27, 2006. This discussion is supported by copies of source documents in the attached exhibits. As explained there, the delay in executing the final agreement with BMP

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2087-E to clarify that the Black Mesa Pipeline costs are fuel-related and may be recorded in the ERRA. This advice letter was approved effective February 4, 2007 by an Energy Division letter dated July 6, 2007.

<sup>44</sup> June 28 Supplemental Testimony, page 4.

“does not alter the fact that BMPI and SCE had already incurred contractual obligations to each other, with SCE’s obligation being to reimburse BMPI for costs incurred in holding the pipeline staff and facilities in standstill mode from January through March 2006.” The information presented in SCE’s June 28 Supplemental Testimony fully complies with the requirement of Resolution E-4075 that SCE justify the obligation to incur the standstill agreement costs.

In its August 3 Report, DRA did not discuss SCE’s presentation of these Mohave fuel-related costs in this proceeding. However, as noted above, DRA did find SCE’s URG operations to be “satisfactory.”

Accordingly, SCE requests the Commission to find that its costs related to SCE-owned coal fired generating resources, including the Mohave fuel-related costs, were reasonable.

#### **C. Catalina Diesel Operations**

SCE set forth the reasonableness of its Catalina Island diesel operations in Chapter Six of Exhibit SCE-1. On page 3-4 of its Report, DRA noted that every three years, “SCE negotiates, through a competitive bidding process, a contract with a supplier [for Catalina] at the lowest cost available. As a member of the Procurement Review Group (PRG), DRA is aware of SCE’s efforts to minimize fuel costs. DRA finds SCE procurement activities to be reasonable.”<sup>45</sup>

SCE requests the Commission to find SCE’s Catalina Diesel operations reasonable.

#### **D. Utility Contract Administration and Costs**

In Chapter Eight of Exhibit SCE-1, SCE showed that in administering its procurement contracts during the Record Period, it acted consistent with the contract terms and conditions, in good faith, and in accordance with the Commission’s directives and recommendations. SCE’s testimony in Chapter Eight included a discussion of its net collateral fees incurred during the Record Period, which totalled \$6,038,827.<sup>46</sup>

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<sup>45</sup> DRA Report at page 3-4, lines 6-10.

<sup>46</sup> Exh. SCE-1 at pages 172-180.



DRA reviewed the administration and costs of SCE's non-qualified facilities (Non-QF) contracts, including SCE's net collateral fees incurred during the Record Period, and concluded that "SCE's ongoing Non-QF contract administration activities have been conducted in a prudent manner."<sup>47</sup> DRA therefore recommended "that SCE's requests in [its] Application for the Commission to find [SCE's] Non-QF contract administration activities reasonable be granted."<sup>48</sup>

Accordingly, SCE seeks a finding by the Commission that it prudently and diligently administered its Non-QF contracts during the Record Period.

#### **E. PURPA Contract Administration and Costs**

In Chapter Nine of Exhibit SCE-2, SCE demonstrated that it administered its PURPA<sup>49</sup> contracts in a reasonable manner and in accordance with Commission standards. DRA reviewed SCE's management and administration of its PURPA contracts, and based on its review, recommended that "the Commission find SCE's administration and management of its 251 PURPA QF contracts reasonable and SCE should be authorized to recover the costs associated with the PURPA QF contracts."<sup>50</sup>

Accordingly, SCE requests the Commission to find SCE's administration and management of its PURPA contracts to be reasonable.

#### **F. Operation of Ratemaking Accounts**

In Chapter Twelve of Exhibit SCE-2, SCE detailed the operation of the various ratemaking accounts to assist the Commission in its review and audit of SCE's balancing account and other regulatory account activities.

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<sup>47</sup> DRA Report at page 5-1, lines 7-8.

<sup>48</sup> *Id.* at page 5-1, lines 10-11.

<sup>49</sup> PURPA stands for Public Utility Regulatory Policies Act of 1978. PURPA contracts are also known as Qualifying Facility Contracts.

<sup>50</sup> DRA Report at page 4-13, lines 2-5.

With the exception of the MBA,<sup>51</sup> DRA reviewed SCE's ratemaking account operations and entries and found that "[n]o items of a material nature requiring adjustments were noted."<sup>52</sup> Accordingly, DRA concluded that "SCE's requested net revenue increase in 2008 of \$4.863 million...is reasonable, accurately recorded, and recoverable."<sup>53</sup> Therefore, SCE requests that the Commission find that the entries recorded in these balancing accounts and other regulatory accounts are appropriate, correctly stated, and in compliance with Commission decisions.

## V.

### **SUMMARY OF ISSUES NOT ADDRESSED IN DRA'S REPORT**

#### **A. Renewables Portfolio Standards Contract Administration and Costs**

SCE originates certain power purchase agreements pursuant to California's renewables portfolios standard (RPS) legislation, which became effective on January 1, 2003. For ease of reference, these agreements are referred to as "RPS contracts." As noted in Chapter Ten of Exhibit SCE-2, "The Commission resolutions approving the RPS contracts typically provide for the recovery of all payments made pursuant to those contracts, subject to the Commission's review of the reasonableness of SCE's contract administration."<sup>54</sup>

Accordingly, in Chapter Ten of Exhibit SCE-2, SCE set forth its RPS contract-related expenses, described its RPS contract development and administration activities during the Record Period, and demonstrated that such activities were reasonable and in accordance with all applicable standards. SCE therefore requests that the Commission find its administration and management of its RPS contracts reasonable and the associated \$98.8 million cost recoverable.<sup>55</sup>

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<sup>51</sup> As noted above, the MBA was excluded from review in this proceeding pursuant to the June 4th Ruling.

<sup>52</sup> DRA Report at page 6-7, lines 8-9.

<sup>53</sup> *Id.* at page 6-7, lines 11-14.

<sup>54</sup> Exh. SCE-2 at page 49, lines 7-11.

<sup>55</sup> *Id.* at pages 49-50.

**B. California Independent System Operator (CAISO)-Related Costs**

As set forth in Chapter Eleven of Exhibit SCE-2, SCE incurred approximately \$262.9 million in CAISO-related costs during the Record Period.<sup>56</sup> The majority of these CAISO-related costs were unavoidable. Those costs that SCE had limited discretion to control were managed consistent with the objective of minimizing costs to bundled customers.<sup>57</sup> DRA has not challenged SCE's request that the Commission find all CAISO-related costs incurred during the Record Period to be reasonable. Accordingly, the Commission should make such a finding.

**C. Special Sales Contract Administration and Costs**

SCE set forth the results of its administration of its two remaining Self Generation Deferral Rate (SGDR) agreements, with ExxonMobil and Tosco (also known as ConocoPhillips), in Chapter Thirteen of Exhibit SCE-2. DRA has not challenged SCE's testimony regarding the reasonableness of its administration of these SGDR agreements. Accordingly, SCE requests that the Commission find that SCE's administration of these SGDR agreements during the Record Period was reasonable.

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<sup>56</sup> *Id.* at page 57, line 4.

<sup>57</sup> *Id.* at page 59, lines 16-17.

## VI.

### CONCLUSION

For all the reasons stated herein, SCE respectfully requests the Commission to grant the relief it has requested on all the issues discussed above, and to adopt the proposed findings of fact, conclusions of law, and ordering paragraphs set forth in Appendix A.

Respectfully submitted,

/s/Connor J. Flanigan

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October 12, 2007

**APPENDIX A**

**Findings of Facts of Southern California Edison Company**

## **APPENDIX A**

### **Findings of Fact**

1. Southern California Edison Company (SCE) filed this Energy Resource Recovery Account (ERRA) application on April 2, 2007. The application appeared in the Commission's Daily Calendar on April 5, 2007.
2. SCE's application seeks Commission review of its utility retained generation (URG) expenses, its administration of power purchase agreements, its least-cost dispatch activities and related spot market transactions, and its procurement-related revenue and expenses recorded in its ERRA Balancing Account, for the period beginning January 1, 2006 and ending December 31, 2006 (Record Period).
3. As of the close of the Record Period, SCE's ERRA Balancing Account reflected \$4.255 billion in expenses and an overcollection of \$526 million.
4. SCE seeks recovery of a net undercollected balance of \$4.863 million in four memorandum accounts (Exhibit SCE-2, page 62).
5. SCE seeks a Commission finding that the amounts shown in the above accounts, as well as all other regulatory accounts set forth in Exhibit SCE-2, Chapter XII, are reasonable, appropriate, correctly stated, and in compliance with all relevant Commission decisions.
6. SCE's application also seeks a finding that the entries recorded in the Mohave Balancing Account (MBA) are reasonable, and that capital-related expenditures of \$16.4 million that SCE incurred to preserve the possibility of continued or resumed operations at the Mohave Generating Station (Mohave) beyond December 31, 2005 are reasonable and recoverable.
7. On May 7, 2007, the Division of Ratepayer Advocates (DRA) filed a motion to strike SCE's testimony related to the MBA, arguing that Commission consideration of the O&M and capital-related expenses in the MBA was beyond the scope of the ERRA

proceeding. SCE filed its opposition to DRA's motion on May 22, 2007, noting that the MBA tariff requires that the MBA be reviewed in the ERRA proceeding.

8. On June 4, 2007, the Commission issued its Scoping Memo in which it ruled that it would not include review of the MBA in this proceeding because SCE had not yet addressed the permanent status of Mohave, as required by Ordering Paragraph 9 of D.06-05-016. After SCE addresses the permanent status of Mohave, a determination will be made regarding the appropriate proceeding for reviewing the MBA.

9. The Scoping Memo did not exclude Commission review in this proceeding of the Mohave fuel-related costs that are recorded in the ERRA Balancing Account.

10. On August 3, 2007, DRA submitted its "Report on Southern California Edison Company's 2006 Energy Resources Recovery Account (ERRA)" in this proceeding.

11. The scope of DRA's review in its August 3 Report concentrated on least-cost dispatch activities, utility-retained generation operations and fuel expenses, contract administration of qualifying facilities (QF contracts) and non-qualifying facilities (Non-QF contracts), and an audit of SCE's ERRA Balancing Account entries.

12. DRA's August 3 Report did not recommend any disallowances, but it did raise concerns relating to SCE's administration of least-cost dispatch principles and the reasonableness of SCE's nuclear generation and fuel expenses incurred during the Record Period.

13. On September 7, 2007, SCE filed its rebuttal testimony, Exhibit SCE-4, in which it responded to the concerns DRA raised in its August 3 Report.

14. Exhibits SCE-1, SCE-2 and SCE-4 provided detailed support regarding the appropriateness of SCE's least-cost dispatch methodology and the reasonableness of SCE's nuclear generation and fuel expenses incurred during the Record Period.

15. Chapter II of Exhibit SCE-1 and the accompanying Appendices A and B describe the methodology SCE employed in making least-cost dispatch decisions during the

Record Period. This is a reasonable and appropriate methodology for SCE to comply with Standard of Conduct Four, the Commission's adopted least cost dispatch standard.

16. The "monthly average" price comparison methodology utilized in Chapter Two of DRA's August 3 Report is deficient because it does not purport to do any of the following: i) account for the different prices of the various mixes of product types that SCE purchases and sells, ii) distinguish time frames during which SCE purchases and sells power, iii) account for the different delivery locations at which SCE purchases and sells power, or iv) consider the differences in the underlying prices of natural gas that largely drive the price of spot electricity that SCE purchases and sells.

17. The prices at which transactions are consummated between a willing buyer and a willing seller are, in fact, "real" market prices.

18. Most active markets are influenced by speculators and the extent (if any) of speculators' influence on the gas market is unknowable.

19. SCE had a robust hedging program in place during 2006 to protect its customers from excessive price increases.

20. SCE set forth the reasonableness of the San Onofre Nuclear Generating Station (SONGS) generation and nuclear fuel expenses it incurred during the Record Period in Chapter Seven of Exhibit SCE-2 and Chapter Three of Exhibit SCE-4.

21. The 26.2 percent reduction in the combined SONGS output from 2005 to 2006 resulted from the fact that neither SONGS unit had a refueling and maintenance outage during 2005, whereas both units had such outages in 2006, as well as a mid-cycle maintenance outage on Unit Three.

22. SCE also set forth the reasonableness of the Palo Verde Nuclear Generating Station (Palo Verde) generation and nuclear fuel expenses it incurred during the Record Period in Chapter Seven of Exhibit SCE-2 and Chapter Three of Exhibit SCE-4.



23. Although SCE (like the other Palo Verde co-owners) is an Nuclear Regulatory Commission (NRC) licensee at Palo Verde, neither SCE nor the other Palo Verde co-owners has authority to approve or disapprove operational decisions at Palo Verde.
24. Only the licensed operating agent for Palo Verde, Arizona Public Service (APS), has authority to make operational decisions at the plant.
25. On March 7, 2007, the NRC issued an annual assessment letter regarding Palo Verde, which expressed a number of concerns regarding the safety of operations at the facility. However, none of the concerns raised by the NRC had any impact at all on the existence or duration of any outages at any of the three Palo Verde units during the Record Period. The concerns raised in the NRC assessment letter therefore had no impact on the cost of the replacement power SCE incurred during Palo Verde outages.
26. Beginning in late December 2005, APS experienced increased levels of vibration on shutdown cooling valve SI-651 after APS restarted Palo Verde Unit One following a scheduled shutdown for the installation of new steam generators.
27. The level of excess vibration on SI-651 could not have been anticipated.
28. Solving the excess vibration issue proved to be extremely complicated. APS spent several months pursuing a number of alternatives to resolve the issue and brought in experts from both the nuclear industry and academia to assist APS with its efforts.
29. The excess vibration issue was finally resolved when APS relocated SI-651. Relocating SI-651 was a complex and challenging modification requiring extensive engineering efforts.
30. Although APS was able to solve the excess vibration issue, it has not been able to establish a root cause for why the excess vibration occurred in the first place. Because the configuration of Units 2 and 3 is similar to Unit 1, APS has notified the co-owners that it plans to do the same modification to Units 2 and 3 as a pre-emptive measure to prevent any possible future vibration issues at those units.

31. On September 19, 2006, Palo Verde Unit One was manually shut down following the failure of a pressurizer heater, discovered the day before. The pressurizer heater was manufactured by a company called Watlow, procured by Westinghouse.

32. This was not the first heater failure at Unit One. APS had experienced prior failures with the Watlow-manufactured pressurizer heaters at Unit One, resulting in an unacceptable failure rate involving the Watlow heaters.

33. Watlow was unable to provide sufficient assurance that the heaters would be able to perform their intended safety function during an accident. As a result, APS decided that the total replacement of these heaters was necessary to avoid further safety issues. APS replaced all 36 Watlow heaters at Unit One during the outage (one heater had to be abandoned in place).

34. Since the total replacement of the Watlow heaters, the pressurizer heaters at Unit One have operated with no further problems.

35. On October 21, 2006, Unit One automatically shut down due to an anomaly with a control element assembly (i.e., control rod) reed position switch signal.

36. The reactor shutdown was uncomplicated, meaning that all components functioned as required and there were no other problems. While troubleshooting, APS found a loose connector going to the control element assembly, which caused the anomaly. The cable connector was visually inspected and reconnected, which cleared the problem.

37. APS took a number of actions in response to this event, including: i) revision of operating procedures to include new actions operators should take when core protection calculator indications are erratic, ii) a historical review of similar cables to see if any additional actions should be taken (replacement, repair, etc.), and iii) simulator training to ensure operators understand the newly revised procedures.

38. Since reconnecting the cable connector, Unit One has experienced no further problems related to this issue.

39. DRA took no exception to SCE's operation and costs of its hydroelectric facilities during the Record Period.
40. DRA took no exception to SCE's operation and costs of its SCE-owned coal-fired generating resources during the Record Period.
41. DRA took no exception to SCE's Catalina Island diesel operations and costs incurred during the Record Period.
42. DRA took no exception to the administration and costs of SCE's Non-QF contracts during the Record Period.
43. DRA took no exception to the administration and costs of SCE's QF contracts (also known as PURPA<sup>1</sup> contracts) during the Record Period.
44. With the exception of the MBA, which was excluded from review in this proceeding, DRA took no exception to any of SCE's ratemaking account operations and entries set forth in Chapter XII of Exhibit SCE-2.
45. DRA took no exception to the Mohave fuel-related expenses recorded in the ERRA Balancing Account.
46. DRA did not address SCE's Renewables Portfolio Standards (RPS) contract administration and costs incurred during the Record Period.
47. DRA did not address SCE's California Independent System Operator (CAISO)-related costs incurred during the Record Period.
48. DRA did not address SCE's administration of its Self-Generation Deferral Rate (SGDR) agreements with ExxonMobil and Tosco (also known as ConocoPhillips).

### **Conclusions of Law**

1. SCE's administration of its procurement contracts during the Record Period was reasonable and prudent.

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<sup>1</sup> PURPA stands for Public Utility Regulatory Policies Act of 1978.

2. During the Record Period SCE consistently dispatched the resources and contracts under its control and made spot market transactions in a manner that complied with the Commission's adopted standard, Standard of Conduct No. Four.
3. In regulating nuclear plant operations, including operations at Palo Verde, the NRC's primary concern is to protect the public health and safety.
4. In reviewing SCE's utility-retained generation operations (including SONGS and Palo Verde) and related fuel expenses in this ERRA proceeding, the Commission's primary concern is whether the cost of the replacement power SCE purchased as a result of outages during the Record Period was reasonable.
5. SCE's hydroelectric facilities were operated in a prudent manner during the Record Period.
6. SCE's operation of its SCE-owned coal-fired generating resources during the Record Period was reasonable.
7. SCE's diesel fuel and transportation costs associated with its Catalina Island operations were reasonable and recoverable.
8. SCE's nuclear generation, nuclear fuel expenses, and fuel material and services that SCE purchased for both SONGS and Palo Verde during the Record Period were reasonable and recoverable.
9. SCE's cost of replacement power it purchased during scheduled and unscheduled outages at its URG facilities during the Record Period was reasonable and recoverable.
10. SCE prudently administered its Non-QF contracts during the Record Period. SCE's costs associated with the administration of its Non-QF contracts during the Record Period were reasonable and recoverable.
11. SCE administered its QF contracts prudently and in accordance with the Commission's established standards. SCE's costs associated with the administration of its QF contracts were reasonable and recoverable.

12. SCE prudently and reasonably administered its RPS contracts during the Record Period. SCE is thus entitled to recover its costs associated with its RPS contracts, which totaled \$98.8 million during the Record Period.
13. SCE's CAISO-related costs incurred during the Record Period, which total approximately \$262.9 million, are reasonable and recoverable.
14. SCE's ERRA Balancing Account and all other regulatory account entries set forth in Chapter XII of Exhibit SCE-2 are accurately stated and reasonable.
15. SCE's requested revenue increase of \$4.863 million associated with the four memorandum accounts shown in Table XII-18 on page 62 of Exhibit SCE-2 is reasonable and should be adopted.
16. SCE's administration of its SGDR agreements during the Record Period was reasonable.
17. Information placed under seal should remain sealed.
18. This decision should be effective today, in order to allow the docket to be closed expeditiously.

## **ORDER**

### **IT IS ORDERED** that:

1. SCE's administration of its power purchase agreements and least-cost dispatch activities during the period beginning January 1, 2006 and ending December 31, 2006 was reasonable and prudent.
2. SCE's diesel fuel and transportation costs associated with its Catalina Island operations during the Record Period were reasonable and recoverable.
3. SCE's nuclear generation, nuclear fuel expenses, replacement power costs, and fuel material and services that SCE purchased for both SONGS and Palo Verde during the Record Period were reasonable and recoverable.

4. SCE's costs associated with the administration of its Non-QF contracts incurred during the Record Period were reasonable and recoverable.
5. SCE's costs associated with the administration of its QF contracts during the Record Period were reasonable and recoverable.
6. SCE is entitled to recover its costs associated with its RPS contracts, which totaled \$98.8 million during the Record Period.
7. SCE's CAISO-related costs incurred during the Record Period, which totaled approximately \$262.9 million, were reasonable and recoverable.
8. SCE's requested revenue increase of \$4.863 million associated with its four ratemaking accounts is reasonable and should be adopted.
9. SCE is authorized to eliminate the Employee-Related Balancing Account and the Direct Access Customer Charge Revenue Memorandum Account from its Preliminary Statements.
10. All information placed under seal shall remain sealed.
11. Application 07-04-001 is closed.

This order is effective today.

Dated \_\_\_\_\_, at San Francisco, California.

**CERTIFICATE OF SERVICE**

I hereby certify that, pursuant to the Commission's Rules of Practice and Procedure, I have this day served a true copy of the **OPENING BRIEF OF SOUTHERN CALIFORNIA EDISON COMPANY (U-338E)** on all parties identified on the attached service list(s). Service was effected by one or more means indicated below:

Transmitting the copies via e-mail to all parties who have provided an e-mail address.  
First class mail will be used if electronic service cannot be effectuated.

Executed this **12<sup>th</sup> day of October, 2007**, at Rosemead, California.

/s/ Christina A. Sanchez  
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**A.07-04-001**

Friday, October 12, 2007

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